BRIEF IN SUPPORT OF PETITION.

Opinion Below.

The opinion below is reported in 387 Ill. Supreme Court Reports, at page 241.

Jurisdiction.

The jurisdiction of this Court is invoked under Section 237(b) of the Judicial Code, as Amended by the Act of February 13, 1926, Section 344 Title 28 U. S. C. A.

Petitioners seasonbly have raised the constitutional question to the effect that Section 2(e)(5) of the Illinois Unemployment Compensation Act, (Ill. Rev. Stat. 1943, Chap. 48, par. 218) is repugnant to Section 1 of Article 14 of the Amendments to the United States Constitution (R. 29, 35). This petition for the issuance of the Writs of Certiorari is filed prior to the expiration of three months from September 18, 1944, the date when the Petition for Rehearing in the Supreme Court of Illinois was denied (R. 43).

Statement of the Case.

On January 7, 1942, there was rendered a report of the representative of the Director of Labor of the State of Illinois, finding that on June 5, 1941, these Petitioners, together with Insul-Mastic Laboratories, Inc., were employers liable for the payment of contributions under the Illinois Compensation Act, and that they were assessed thereunder (R. 4, 5, 6). The pertinent portions of the Unemployment Compensation Act have been heretofore set forth in the Petition for Certiorari. The entire Act appears in Illinois Rev. Stat. 1943, Chap. 48, Paragraphs 217-250.

A stipulation was entered into between the Director of

Labor and the Petitioners, pertinent portions of which are as follows (R. 7, 8, 9):

"(2) That said corporations were, from the date of their incorporation and throughout the periods included in the Director's determinations and assessments, controlled either directly or indirectly by legally enforceable means or otherwise by one O. V. McGrew; that each of said corporations, if treated as a single employing unit together with the other corporations had in its employment a sufficient number of persons to constitute it an employer liable for the payment of contributions under Section 2(e)(1) of the Illinois Unemployment Compensation Act.

"(3) That none of the corporations from the period of their incorporation throughout the period covered by the Director's determinations and assessments, employed in their individual corporate capacity a sufficient number of persons so as to become liable for contributions as an employer under the provisions of Section (2)(e)(1)(A) or (2)(e)(1)(B) of the Illinois Unemployment Compensation Act.

"(4) Except for the facts herein contained there is no evidence that any of the above mentioned corporations were incorporated or formed for the purpose of evading the payment of contributions under the Illinois Unemployment Compensation Act, as amended.

"(5) That the amounts set forth under the caption 'Wages Payable' in each and all of the determinations and assessments by the Director of Labor (incorporated in this stipulation by reference and identified as Director's Exhibits No. 3 in each of the above causes) are correct.

"(6) That the shareholders, together with their respective shareholdings or percentage of shareholdings in said corporations, are as follows:

McGrew Paint & Asphalt Co., a corporation

O. V. McGrew, 4998 shares of common stock
V. B. McGrew, 1 share of common stock
Robert E. McComas, 1 share of common stock
Genevieve McGrew, 500 shares of preferred stock

Dednox, Inc., a corporation

O. V. McGrew, 55% of capital stock
Joseph G. Slottow, 25% of capital stock
M. R. Becker, 5% of capital stock
Jay R. Sheesley, 15% of capital stock

Railway Paint Company, a corporation

O. V. McGrew, 55% of capital stock
Joseph G. Slottow, 25% of capital stock
M. R. Becker, 5% of capital stock
Jay R. Sheesley, 15% of capital stock

Insul-Mastic Roofing & Siding Co., a corporation

O. V. McGrew, 547 shares of capital stock
Fred Cox, 350 shares of capital stock
V. B. McGrew, 100 shares of capital stock
G. L. Burton, 1 share of capital stock
H. P. Shane, 1 share of capital stock
J. M. Rusteck, 1 share of capital stock

Insul-Mastic Laboratories, Inc., a corporation

O. V. McGrew, 247 shares of capital stock
Genevieve McGrew, 250 shares of capital stock
V. B. McGrew, 200 shares of capital stock
Fred Cox, 50 shares of capital stock
G. L. Burton, 1 share of capital stock
J. M. Rusteck, 1 share of capital stock
H. P. Shane, 1 share of capital stock
D. Paley, 250 shares of capital stock."

Objections to the report were filed and the Director of Labor overruled and adopted the report of his representative (R. 9-12).

The causes were reviewed by the Circuit Court of Cook County on Certiorari. The reports were all approved and it was ordered that the Writs of Certiorari be quashed and judgments were entered against your Petitioners (R. 12-16).

An appeal was taken to the Supreme Court of Illinois, and its opinion appears on pages 29 to 35 in this Record.

The Stipulation constitutes by its own provisions the complete record of the proceedings (R. 9).

Specifications of Errors to Be Urged.

The judgments of the Supreme Court of Illinois should be reversed because they are based upon Section 2(e) (5) of the Illinois Unemployment Compensation Act, which violates Section 1, Article 14 of the Amendments of the Constitution of the United States in two respects: First, in that it provides for the taxation of a group of employing units collectively where individually none of them would be subject to taxation, the only basis for their liability as a group being that they are owned or controlled by the same interests by *legally enforcible means or otherwise.* The stipulation shows that O. V. McGrew while owning a majority of the capital stock of the petitioning corporations did not own all of the capital stock of each of the petitioning corporations but only a majority, and, therefore, the corporations must be held liable if at all under the stipulation where it is agreed that he controls the petitioning corporations by "legally enforceable means or otherwise." Secondly, the statutory provision in question is obnoxious to Section 1, Article 14, of the Amendments of the United States Constitution because the provision is arbitrary, unreasonable, denies the Petitioners the equal protection of the laws, and the decision of the Court below sustaining the provision, results in the taking of the property of the Petitioners without due process of law regardless of the nature of the control, whether by "legally enforceable means or otherwise."

ARGUMENT.

I.

The affiliate provision of the Illinois Unemployment Compensation Act, being Section 2(e)(5) thereof (Ill. Rev. Stat. 1943, Chap. 48, par. 218) violates Section 1 of Article 14 of the Amendments of the United States Constitution, insofar as it purports to bring together for taxation purposes employing units (which singly are not subject to the tax) merely because they are "controlled either directly or indirectly by legally enforceable means or otherwise."

As has been pointed out heretofore all of the evidence is contained in the stipulation entered into between the parties (R. 6 to 9). From this stipulation it appears that (R. 7) not one of these Petitioners for the period in question had employed in its individual capacity a sufficient number of persons so as to become liable as employer for contributions under the appropriate sections of the Act. This stipulation also, however, following the words of the Statute (R. 7), provided that collectively these Petitioners together with a fifth corporation, Insul-Mastic Laboratories, Inc., if considered as a single employing unit, had in their employment a sufficient number of persons to render them liable for payments of contribution. That during the taxable period they were "controlled either directly or indirectly by legally enforceable means or otherwise" by one O. V. McGrew.

The clause governing the enforceability of the means of control is clearly contrary to public policy and is unconstitutional. It manifestly purports to cover control by means otherwise than those legally enforceable. The stipulation

fails to disclose whether or not O. V. McGrew's alleged control arises out of legal means of enforcement or is illegal in its nature. Such a stipulation would cover any situation whereby O. V. McGrew controls these Petitioners by illegal threats or any sort of fraudulent or unlawful scheme. Instances of such control may be called to mind without difficulty and need not be mentioned here whether they arise from business duress or any other type of duress or fraud.

The stipulation (R. 8) discloses that there are ten other shareholders in these corporations aside from O. V. McGrew. Some of them hold substantial interests therein, for example, in McGrew Paint & Asphalt Company, Genevieve McGrew holds 500 shares of preferred stock, and in Dednox, Inc., Joseph G. Slottow holds 25% of the capital stock. Joseph G. Slottow also holds 25% of the capital stock of the Railway Paint Company. Fred Cox holds 350 shares and V. B. McGrew holds 100 shares of the capital stock of the Insul-Mastic Roofing & Siding Company. It may be argued, although from the stipulation it does not so appear, and such assumption would not be warranted from the Record, that the actual control of O. V. McGrew is by acquiescence of the other shareholders. This type of control is too vague, indefinite and unreasonable to form the basis for any legal concept upon which to base an assessment.

The record refutes the possibility that ownership is the basis of control. O. V. McGrew's ownership varied in all of these corporations. For example, he owned 55% of the capital stock of the Railway Paint Company, but he also owned 4,998 shares of the common stock out of a total issue of 5000 in the McGrew Paint & Asphalt Company. In the Insul-Mastic Roofing & Siding Co., he owned 547 shares of the capital stock out of a total issue of 1000 shares.

In discussing a somewhat analogous situation arising out of the problem of consolidated returns of affiliated corporations under the Federal Statute (40 Stat. at L. 1081, Chap. 18, Par. 240(b)), this Court indicated in *Handy & Harmon* v. *Burnet*, 284 U. S. 136, at page 140, that assuming that there was actual control of the corporations there involved to distinguish it from legal control, affiliation would make for inequality unless the beneficial owners have substantially all of the stock of each of the said corporations. The Court there held that control without legally enforceable means could mean without title, beneficial ownership or legal means to enforce it. That control resting solely on acquiescence, the exigencies of business or other considerations having no binding force are not sufficient to satisfy the statute. The Supreme Court of the United States in this last mentioned opinion construed the Federal Statute to cover a situation where legal control only was involved, but it is clear from its opinion that any other type of control could not legally furnish a basis for a consolidated tax of the corporations.

That ownership of a majority of the stock in the corporations could not form the basis of the judgments below is clear from the opinion of the Court and from the stipulation which is not based upon ownership but on control "by legally enforceable means or otherwise" and under this stipulation no presumption may be indulged in to the effect that the control was legally enforceable and not otherwise.

The general principles as to the constitutionality or unconstitutionality under Section 1 of the 14th Amendment, have been so frequently discussed that it is not deemed necessary to enlarge on them at length in this brief. As

was stated in *Connolly* v. *Union Sewer Pipe Co.*, 184 U. S. 540, at page 689:

> "What may be regarded as a denial of the equal protection of the laws is a question not always easily determined, as the decisions of this court and of the highest courts of the states will show. It is sometimes difficult to show that a state enactment, having its source in a power not controverted, infringes rights protected by the national Constitution. No rule can be formulated that will cover every case. But upon this general question we have said that the guaranty of the equal protection of the laws means 'that no person or class of persons shall be denied the same protection of the laws which is enjoyed by other persons or other classes in the same place and under like circumstances.' "

The Court further said, page 690:

> "The difficulty is not met by saying that, generally speaking, the state when enacting laws may, in its discretion, make a classification of persons, firms, corporations, and associations, in order to subserve public objects. For this court has held that classification 'must always rest upon some difference which bears a reasonable and just relation to the act in respect to which the classification is proposed, and can never be made arbitrarily and without any such basis. * * * But arbitrary selection can never be justified by calling it classification. The equal protection demanded by the 14th Amendment forbids this. * * * No duty rests more imperatively upon the courts than the enforcement of those constitutional provisions intended to secure that equality of rights which is the foundation of free government. * * *' "

In *Royster Guano Co.* v. *Virginia*, 253 U. S. 412, this Court said at pages 990, 991, concerning a Statute of the State of Virginia, exempting the burden of an income tax from certain corporations and under certain circumstances:

> "It is unnecessary to say that the 'equal protection of the laws' required by the 14th Amendment does not

prevent the states from resorting to classification for the purposes of legislation. Numerous and familiar decisions of this court establish that they have a wide range of discretion in that regard. But the classification must be reasonable, not arbitrary, and must rest upon some ground of difference having a fair and substantial relation to the object of the legislation, so that all persons similarly circumstanced shall be treated alike."

II.

Aside from the clause "by legally enforceable means or otherwise", Section 2(e)(5) of the Illinois Unemployment Compensation Act is as a whole obnoxious to the provisions of Section 1, Article 14 of the Amendments of the Constitution of the United States.

We come now to the question as to whether or not even if the control is by legally enforceable means the affiliate provision above referred of the Illinois Unemployment Compensation Act is constitutional. It is the contention of these Petitioners that it is not constitutional, that it violates the equal protection of the laws and deprives them of their property without due process of law. The stipulation (R. 8) shows that the minority stockholders in these corporations do not hold a nominal number of shares but very substantial interests therein, for example, in the McGrew Paint & Asphalt Co., one minority shareholder owns all of the 500 shares of preferred stock. In Dednox, Inc. and in Railway Paint Company, the minority shareholders hold 45% of the capital stock. In Insul-Mastic Roofing & Siding Company, they hold 453 shares out of a total issue of 1000 shares of the capital stock. These minority shareholders and the corporations in which they hold their stock are penalized by the judgment below on this Record, merely

because O. V. McGrew owns a majority of the shares of stock of other corporations.

In the case of *Independent Gasoline Co.* v. *Bureau of Unemp. Comp.*, 190 Ga. 613, 10 S. E. (2d) 58, the Court said at page 616:

> "But it is contended that the legislature was authorized to place this defendant in a classification different from similar corporations and individuals, because of the fact that the owner of a majority of its stock owns a majority of the stock of another corporation, and that the two corporations are controlled by the same interests. This reasoning ignores the fact that this defendant is utterly powerless to determine who shall own its capital stock, or to fashion the business transactions and conduct of its stockholders. Since these are matters beyond the control of the corporation, they do not constitute a basis justifying the classification; and a classification must be reasonable and have a fair and substantial relation to the object of the legislation."

This Court has denied certiorari in this case. (See *Bureau of Unemp. Comp., Petitioner,* v. *Independent Gasoline Co.*, 311 U. S. 707.)

In the case of *Benner-Coryell Lumber Co.* v. *Indiana Unemployment Comp. Board,* 218 Ind. 20, 29 N. E. (2d) 776, the Court said at page 780:

> "Over the sale and transfer of its stock, a corporation ordinarily has no control. Transactions relating to the sale of capital issues may be negotiated privately or through independent marketing agencies, and the responsible officers of a corporation may not be advised as to the ownership of its shares until the certificates therefor are presented for transfer. The stock of a particular corporation may be so distributed that the controlling majority thereof may change ownership at frequent intervals. In practical operation, situations may arise where the majority of the voting stock may or may not be in the hands of the same interests many

times between annual meetings of the stockholders, or even between the tax paying periods. Under such circumstances, uncertainty and confusion would be inevitable and a continuity of policy impossible. For these reasons, it seems impossible to justify the interpretation sought by the state, upon the theory that the holders of a majority of the stock have control thereof because it is within their power to dictate who the directors shall be."

This Court has also denied Certiorari in the Indiana case (see *Indiana Unemployment Comp. Board, Petitioner*, v. *Benner-Coryell Lumber Co.*, 312 U. S. 698). It needs little further argument to indicate that the Illinois Statute is arbitrary and oppressive. It is discriminatory against the Petitioners, who, individually, would be exempt from the tax. It is also discriminatory against the minority stockholders of these corporations. It is admitted in the stipulation (R. 8, Par. 4) that there is no evidence that the corporations were incorporated or formed for the purpose of evading the payment of the tax, except for the facts contained in the stipulation. There never could have been such a contention because the corporations were all in existence before the enactment of the statute complained of.

Conclusion.

It is, therefore, respectfully submitted that the application herein for the Writs of Certiorari to the Supreme Court of Illinois be granted.

Respectfully submitted,

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